

The Co-operative Option

How to Keep Our Power
Australian Owned
and
Community Controlled

**Southern Energy Co-operative
Ltd
1995**

There are two broad responses to the privatisation of Victoria's electric industry:

Political response e.g., Public First, Trades Hall Council, Uniting Church and Labor Opposition. This approach assumes the desirability and possibility of preventing and/or modifying privatisation. The approach is based on a political solution - citizens persuading the State to adopt better and different policies, legislation and regulation.

Economic response e.g., the Orbost Power Co-operative Ltd, Co-operative Energy Ltd and Southern Energy Co-operative Ltd. This approach is based on the possibility of a direct economic response to privatisation by consumers - rather than depending on the State to act.

The **political response** is, ultimately, easier than the **economic response** because it depends on others who comprise the State to decide and act. The **political response** involves limited obligations for electric consumers.

The **economic response**, however, is embedded in obligations for electric consumers - the obligations of co-operative ownership and control.

Communities are increasingly recognizing that their economic development is dependent on their own efforts - rather than on public and private enterprises which are owned and controlled outside their communities. Governments are abandoning communities to market forces. Co-operatives are a tested response to abandonment. The co-operative movement is already well-established - particularly in rural Victoria.

The restructuring of the electric industry is providing a new co-operative opportunity - instead of allowing investor utilities to take over the industry or hope that the Government will come to its senses. Co-operatives challenge the competitive market - within the market.

The co-operative option recognizes that we need to go beyond political solutions - preventing privatisation and restoring public ownership through changed governments and policies. It recognizes that we have to get the politics out of essential services.

Electric co-operatives empower electric consumers - enabling consumers to choose who provides their power.

Co-operative Context

The co-operative movement is enduring and irreversible. While electric co-operatives are new to Victoria, co-operatives were first established in the 19th Century. In rural Victoria earlier this century co-operative butter factories provided power to their local communities. Electricity supply was decentralized with up to 149 co-operative, private and municipal providers. In 1913 the franchise for electricity supply in Boort was given to the Boort Co-operative Butter Factory and Inc. Co. In 1915 the Heyfield and District Co-operative Butter Factory and Electric Lighting Co Ltd established an electric utility. With the establishment of the State Electricity Commission of Victoria (SECV) in 1918, however, these providers were gradually absorbed by the SECV.

There are more than 1000 co-operatives in Victoria.

The last significant co-operative impetus in Victoria was in the 1940-1960s with credit unions and housing co-operatives. The Victorian Government sponsorship of worker co-operatives in the 1980s collapsed in ambivalence - leaving few surviving worker co-operatives.

The co-operative economic system is an alternative to the public and private economic systems. Co-operatives combine the social objectives of public enterprise with the economic objectives of private enterprise. The co-operative model provides the advantages of both the private (efficiency) and public (service) models while avoiding the disadvantages of the private (profit maximization) and public (bureaucracy) models.

The argument for the co-operative model is essentially an argument for economic democracy. It is

the same philosophical argument that is made for political democracy. The co-operative advantage over public and private business is the explanation for the endurance of co-operatives since the 19th Century. Australia's co-operative movement is already a model of democracy, efficiency and profitability. It is part of a world-wide international movement represented in every Continent - Asia, Africa, the Americas and Europe. Co-operatives differ from other types of business in their purpose, ownership, control and benefits:

- Consumers use business techniques to serve ethical purposes. The philosophy and principles of co-operation, for example, have guided co-operatives since their establishment - establishing accepted rules of action and conduct. Co-operative owned businesses are a movement - not an industry. In contrast, the privatisation critique of public business is that it has mixed commercial and non-commercial objectives. The conflict mix does not exist in consumer businesses with commercial objectives serving a non-commercial goal.
- Co-operative businesses are an extension of the consumption needs of consumers. Co-operative businesses are established for a variety of reasons - improving bargaining power, reducing costs, obtaining products or services, obtaining market access, improving product or service quality and improving incomes. The users of the services provided by the co-operative businesses are its owners and controllers - generating both pricing and allocative efficiencies. Private business provides consumers the possibility of lower prices and/or increased choice. Co-operative businesses enable consumers to own their own business and determine the range of services and choices.
- Co-operative businesses are the most democratic form of business ownership. Co-operative ownership is direct and equitable. There is one vote per member irrespective of their shareholding. While the ownership of a private business is also direct, it is inequitable as it is based on wealth - the number of shares owned. The ownership of a public business is indirect without individual shareholding and, therefore, an incentive for the business to be accountable. Environmentalism has focused on ecologically sustainable development without taking it to its logical conclusion - ecologically sustainable businesses.
- Co-operative businesses are economically and organizationally stable - reflecting and reinforcing local and Australian ownership and the independence of the business. Take-over by Australian and foreign investors and large shareholders is not possible. Private business, however, is subject to take-over, asset-stripping and re-location if deemed profitable by its investor owners. Private business serve capital - not members. Government privatisation programs are selling public agencies to foreign and private investors. Public business is also unstable because successive governments establish their directions and roles - interfering in strategic directions and commercial decisions.
- Co-operative businesses are committed to community development - for their members and their communities. The basis of consumer ownership is community development - consumers taking responsibility and control for their own destinies. Consumer businesses, therefore, reflect and reinforce the social goals of individuals and communities. In contrast, private business is formed to create wealth for investor owners and public business to create dividends for government.

A co-operative is created when people voluntarily come together on the basis of equality and mutuality to promote their socio-economic well-being in a democratic manner and are based on these three principles:

- User-owner: People who own and finance the co-operative are those that use the co-operative.
- User-control: People who control the co-operative are those that use the co-operative.
- User-benefits: The co-operative's sole purpose is to provide and distribute benefits to the users on the basis of their use.

People establish co-operatives to own, control and patronize their own business. Co-operatives promote self-determination through mutual aid. Co-operatives combine democracy with free enterprise - involving an alternative organizational philosophy, structure and practice.

Through co-operatives communities control their own economic institutions and access to services -

reducing their dependency on the public and private sectors. Co-operatives work for their members and their communities - business techniques serve ethical goals. Co-operative businesses are the most democratic form of business ownership. Co-operative ownership is direct and equitable. There is one vote per member irrespective of their shareholding. Co-operative shareholders are members because they want a service - not a profit. Co-operatives are member-driven not capital driven.

Co-operatives are economically and organizationally stable - reflecting and reinforcing local and Australian ownership. The shares are not tradable and, therefore, purchasable by investors privately or on the stockmarket. Take-over by Australian and overseas investors and/or large shareholders is not possible.

The following table summarizes the key characteristics and differences between co-operative, private and public enterprises:

Industry Context

The electric industry is undergoing significant and irreversible change in Victoria. From 1994 Victoria's electricity supply industry was restructured to comprise eight state owned companies:

- An independent company that will monitor and control the wholesale electricity market and ensure the security of the supply system. This body may ultimately belong to the competitive market participants which it will serve.
- A transmission grid company, Power Net Victoria, which will own, maintain and manage the high voltage grid. This is a natural monopoly and will remain state owned.
- Generation Victoria, an interim generation structure comprising generating units which will trade in the market as independent producers. This will be reviewed after one year to develop a more competitive structure based on independent generating companies.
- Five regionally based distribution companies comprising former SECV distribution assets and the 11 municipal electrical undertakings (MEUs). Three will cover metropolitan Melbourne and two will service rural Victoria.

The Victorian Government has said that a key objective is empowerment of the consumer and that "Consumer choice and demand side management can be encouraged through competition in generation and energy retailing, giving consumers an incentive to transfer their electricity consumption from times of high prices to times of low prices. This represents a significant advantage of empowering purchasers in a competitive market."

The argument for competitive markets is self-validating. It assumes that competition drives efficiency and that efficiency empowers consumers through lower prices and better products and services - driven better because of the competitive market. Competition is said to benefit consumers by resulting in a more disciplined and less political use of capital - reducing the volume of community savings used in inefficient public enterprises. Instead, therefore, there is an injection of investor capital and it is assumed this is not political. But, then, investors in an electric utility are interested in maximizing their profits - rather than serving electric consumers. The basis of increased efficiency is enhanced profitability. Foreign owners of Victoria's distribution companies, for instance, may be primarily interested in establishing a strategic basis for making profits in Asia and South-East Asia and learning from a deregulated electric industry. The issue for electric consumers is not about competition but about choice - consumers empowered to choose between what kind of providers and services.

It is interesting that California's Public Utilities Commission is also proposing to restructure its electric industry which is dominated by investor owned utilities. The Commission is committed to allow consumers to benefit from competition through greater choice and, indeed, some consumer and

environmental groups have supported this restructuring.

Given this restructuring of Victoria's electric industry, there are five distinct business opportunities for co-operatives in a restructured electric industry.

- ◆ The first, and most ambitious, is to buy a distribution company (or an interest in). This would involve acquiring the disco distribution and retail license and to trade as the existing entity of Citypower, United Energy, Solaris, Powercor Australia or Eastern Energy. This would involve purchasing a distribution company - the impetus that led to the establishment of Southern Energy Co-operative Ltd. At present SEC does not have a significant and growing membership and, therefore, strategic alliances and loan-raising are irrelevant considerations.
- ◆ The second is to apply for and acquire a retail license from the Regulator General to purchase and retail energy on behalf of the co-operative members and associates. A smart meter, the CAMRI, would enable this to occur.
- ◆ The third is to promote energy savings, conservation and load shifting. This would involve retailing an appropriate package of energy efficient equipment and load shifting from expensive to less expensive costs for energy to the consumer.
- ◆ The fourth is a sub-franchise from one or more of the five distribution companies holding a distribution and retail license. The object and program would be to protect customers and to gain customers from another franchised area on behalf of the contracted disco. A purchasing co-operative would purchase power and associated services for its members. It is estimated that the viability of a purchasing co-operative depends on a threshold membership of 2000 - with viability increasing with increased membership. A purchasing co-operative would be able to negotiate with distribution companies and generators for the supply of power to its members. If the members underwent long-term contract arrangements with the co-operative, then, long-term contract arrangements would be possible - including supplier installation of smart meters.
- ◆ The fifth is to establish a generation co-operative. While it would be ambitious to attempt to purchase an existing distribution company, it may be possible for a co-operative to become a shareholder in a generation company. What is feasible, however, is the establishment of small power plants of 10MW or less.

Victoria's demand for electricity has steadily increased since the 1960s. Growth is the basic precondition for profitability. The privatisation of the electric industry will accelerate this growth imperative. If demand for electricity does not rise, then, this will place an upper limit on industry profitability and co-operatives will compete for the same dollars and depress the profits of their competitors. Competitive pressures will force utilities to compete for customers to maximize their profitability and, simultaneously, reduce their costs. It is interesting that with the increased threat of competition in the USA their electric co-operatives are beginning to acquire other utilities. Large investor owned utilities are restructuring to lower costs and this includes selling relatively high-cost service areas. For co-operatives, however, purchasing these service areas lower their costs. As at mid-May 1995 there were at least 30 electric co-operatives attempting to purchase neighbouring utilities and it is estimated that within a year the number will be 100.

In 1989-90 electricity generation is estimated to have been responsible for 31% of all Australian Co2 emissions. The rate of energy used in Australia is about 220 Gigajoules per individual per year - compared with the world average of 70 gigajoules. Energy use is an indicator of environment load - indicating the level of physical activities and its input into economic production. It is economically desirable, therefore, to promote both renewable energy sources and energy efficiency.

Co-operative Opportunity

The essence of business viability for an electric co-operative is to strategically attain power in the market - forcing suppliers to negotiate with the co-operative.

Powerful buyers can bargain away and lessen the profits of power providers. They can cause utilities to undercut each other in order to get the business and they can use their power to extract other benefits for electric consumers e.g., renewable energy and energy efficiency programs.

Buyers become powerful in the market when they are few in number and they purchase large quantities, when the consumers' purchases represent a sizable percentage of total sales, when the selling industry comprise large numbers of sellers, when the service is standardized and other suppliers can provide and consumer switch is virtually at zero cost and when it is economically feasible for consumers to purchase from several suppliers. Victoria's restructured electric industry will encourage competition for electric consumers.

What are the industry conditions which impact on the competitiveness of electric co-operatives?

Customer loyalty. There is customer loyalty to a publicly owned SECV and resistance to privatisation and co-operatisation has been based on this loyalty. The gradual privatisation of the electric industry will eliminate this loyalty. Customer loyalty should not, therefore, be an impediment to an electric co-operative. It will be up to all new players, including co-operatives, to earn customer loyalty.

Switching costs. If there is a substantial cost for consumers in switching suppliers, then, this will be an effective barrier to the competitive success of electric co-operatives. Most franchised consumers of a distribution company would, for instance, be unlikely to switch to an electric co-operative if the consumer had to personally purchase a \$1000 smart meter.

Capital costs. The capital costs of becoming and remaining competitive will be critical to an electric co-operative. These costs are essentially threefold - initial and set-up costs, operating costs until a viable market share is secured and the costs imposed on the co-operatives with competitors pricing strategies. If a competitor has significant liquidity reserves, then, it can reduce its margins to drive its competitors out of the industry.

Political barriers. A political framework is established by legislation, regulations, political party policies and the political debate inside and outside the Parliament. This framework can facilitate or hinder electric co-operatives. While there are no legislative or regulative constraints on the co-operative option, the silence of the political parties is a barrier.

Customer mix. The larger the sales volume the lower the cost per Gwh and the higher the proportion of sales to industrial and commercial customers, the lower the unit cost. It has been estimated, for instance, that average operating costs per customer reduce 1.3 cents for every increase of 10 customers.

The Government's commitment to privatisation of the electric industry is a co-operative opportunity. The Government has said that it wishes to empower consumers and is planning to create a competitive market where individual consumers can choose between competing retailers - including all individual householders by December 2000. The Government argues that it is selling the S.E.C.V. to deliver lower electricity prices and better services by giving households and business the freedom from whom they buy their electricity i.e., shop around to get the best deal on electricity. Co-operatives will enable this economic theory to become a purchasing practice - with households and small businesses able to get the best deal. In practice this option is impractical for individual householders but through the volume buying of a co-operative individual electric consumers could have this choice. The more competitive the market, the more competitive electric co-operatives.

An electric utility owned by electric consumers will invariably benefit its members and their communities because the co-operative will return its profits to members as a rebate or through improved services. A co-operative's income is returned to its members and their communities. Electric co-operatives will provide better services than private utilities because its emphasis is on serving the consumer-members - rather than generating profits from consumers for Australian and foreign investors. With privatisation the cost of electricity will either increase or be inflated and service will become erratic and different because of the need to maximize profits for investors. Victoria's distribution company Powercor, in preparation for its privatisation, has already closed or

downsized offices in rural Victoria.

Electric co-operatives are consumer co-operatives - providing an electric service for the member-owners consumption at the greatest possible savings for the members. The electric co-operative impetus in Victoria is a renewal of co-operation - a new form of co-operative.

There are more than 1000 electric co-operatives in the USA owned by 12 million consumer-members. Inspired by this USA example of electric co-operatives working, three electric co-operatives have been established in Victoria since 1992 as follows:

1992 Orbost Power Co-operative Ltd

1994 Co-operative Energy Ltd

1995 Southern Energy Co-operative Ltd

Electric co-operatives are also being proposed for Bacchus Marsh and North East Victoria.

Co-operative Energy Ltd is a member of the Co-operative Federation of Victoria Ltd and Southern Energy Co-operative Ltd has applied for membership.

Business Activity

The first essential is to determine what services will be provided by electric co-operatives. The essential questions are: What services should we offer? Are these services that people really want? What are the relevant industry trends? What prices should we charge for these services? Who will be our customers? Do we understand these customers well? How many of these customers will there be? How will we deliver our services to these customers?

The basic purpose of an electric co-operative must be to reduce costs and improve services for its members. Dependability is basic to both of these.

What are the services that electric co-operatives could offer their members for this will be critical to any decision to join the co-operative.

Membership Base

The strength of a co-operative is its membership - not its financial wealth. A new co-operative does not have the cash reserves to purchase a distribution company and depends, therefore, on three sources for funds - strategic alliances with other businesses who have cash reserves and independent loan-raising capacity, its own membership equity and external loan funds - all are dependent on a significant and growing membership.

Membership growth is dependent on a membership strategy - a marketing plan to recruit members based on the benefits of co-operative membership. The essence of a marketing strategy is the clarity of the marketing plan. The sales strategy that follows the marketing plan must also be consistent with co-operative philosophy and principles.

The decision to become a member must be based on the fact that people form co-operatives to get a service that benefits them individually or contributes to the profitability of their business such as a farm or a shop.

It is a selling strategy based on service. What must underpin the strategy is two considerations:

1. Membership ownership and control.
2. The obligations of membership.

Member ownership and control is not just an optional extra for members - depending on their predilections. It is the core difference between co-operatives and public and private enterprise. The customers of an electric co-operative own the business. The member-owners are concerned about the financial performance of the co-operative, but they are primarily concerned about its services - because of the impact these have on their lives and/or businesses.

Membership of a co-operative imposes obligations on members - because members own and use the co-operative. Members are obligated to patronize their co-operative. The type of co-operative would dictate the nature of the patronage obligation. It may be necessary, for example, to include in the Rules of the co-operative a requirement that members continue to use the services of the co-operative for a specified time period.

There are legal restrictions on the membership recruitment activities of co-operatives. Co-operatives may recruit members but not sell shares.

Two things will underpin the marketing plan - the mission statement and the strategy statement.

Mission statement. The mission statement is a broad statement which would articulate the purpose and rationale for electric co-operatives. It is a why statement - why the co-operative was established for what purpose. The mission statement is particularly important in establishing and maintaining the co-operative philosophy and practice.

Strategy statement. The strategy statement will focus on a co-operative's customer and product focus - how the co-operative will employ its unique strengths and opportunities. The strategy statement will provide the framework for operational decisions - providing the basis for consistency in subsequent decision-making.

Future Projections

In examining this impetus it is important to separate rationalizations from analysis. The factors which could contribute to the growth of support for electric co-operatives could be summarized as follows:

- First, there is the sense of mutual aid - the organizing principle for the establishment and development of co-operatives. Quite clearly, while a majority of Victorians are indicating opposition to privatisation they are not translating this opposition into action. While 20% of Victorians are members of co-operatives, membership can be co-operative specific and not co-operative exclusive. Only a minority of credit union members, for example, use their credit union for their whole of banking purposes.
- Second, there is the role of influentials (e.g., politicians, trade unionists and church leaders) who can influence their direct and indirect constituencies (e.g., political parties, unions and churches) in supporting the electric co-operative option. Attempts by Co-operative Energy Ltd and Southern Energy Co-operative Ltd to engage certain constituencies has elicited no response to date - in particular, the Catholic Commission and the Uniting Church. Meetings with National, Liberal and Labor MPs have elicited in principle and/or practical support for the electric co-operative option.
- Third, there is the issue of co-operation between co-operatives - a basic principle of co-operatives. Since 1992 limited funds have been available through the Australian Association of Co-operatives Ltd, CUSCAL and the Victorian Producers Co-operative Ltd to enable the purchasing of resources and offsetting expenditures. The Co-operative Federation of Victoria Ltd also auspiced the Electric Co-operative Project which preceded the establishment of Co-operative Energy Ltd in 1994.
- Fourth, there is the status of co-operatives in the public debate on ownership options. The debate is crystallized around public or private ownership models and co-operatives are usually identified as a variation of private and/or public ownership - rather than a middle way.
- Fifth, there will be a growing realization that the establishment of electric co-operatives in Victoria is not a temporary phenomena and that the co-operatives are here to stay. There will be individuals and organizations who are not willing to commit themselves to the co-operative option until they are convinced of their ongoing stability.
- Sixth, there will be the realization that the electric industry restructuring is inevitable and irreversible and that the SEC cannot be saved or restored. The restructuring will create a competitive structure and imperative where co-operatives are in the interest of power providers

and consumers.

The electric co-operative impetus is real but small and its growth will be a matter of time. Co-operatives subordinate business techniques to ethical ideas. They eschew politicization through open and voluntary membership and democratic control which establishes the basis for their bipartisanship. The co-operative way is a better way because it is based on member ownership, control and benefit. Co-operatives are us - not them.

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PURPOSE

The aim of the co-operative is to establish an electric co-operative in the United Energy service area.

The co-operative has the preferred object of ownership of United Energy - part, if not full, ownership.

In the meantime, the co-operative will organize electric consumers to bulk purchase cheaper electricity.

MEMBERSHIP

To become a member of Southern Energy Co-operative Ltd, you are required to acquire a minimum of one \$10 share. If you can afford to purchase more shares you are encouraged to do so.

INFORMATION

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